

# State Solid Waste Postclosure and Corrective Action Trust Fund

March 2011

## Background

Assembly Bill 274 (Portantino), Chapter 318, Statutes of 2009, as amended by Assembly Bill 1004 (Portantino), Chapter 417, Statutes of 2010, establishes the State Solid Waste Postclosure and Corrective Action Trust Fund (State Trust Fund). The new statute authorizes solid waste disposal facility operators to elect to participate in the State Trust Fund by paying a quarterly fee of \$0.12 per ton of waste disposed. The fee is projected to raise at least \$18 million over the next ten years to be used to cover the costs of postclosure activities and corrective actions in situations where owners or operators of solid waste disposal facilities fail to perform necessary actions and all financial assurances have been exhausted. The fee does not become operative unless the Department of Resources Recycling and Recovery (CalRecycle) receives, on or before January 1, 2012, letters of participation from landfill operators representing at least 50% of the total annual waste disposal tonnage in 2010.

The total financial exposure posed by environmental threats from landfills is calculated to be as much as \$6.2 billion when projected over the next 100 years. The proposed closure, postclosure maintenance, corrective action, and financial assurances Phase II regulatory changes, operative on July 1, 2010, reduce this total exposure to approximately \$3.2 billion by requiring approximately \$3 billion in financial assurances from landfill operators. There is a reasonable expectation that landfill operators will cover \$2.8 billion of the \$3.2 billion exposure on their own, without providing additional assurances to the state, leaving a projected \$370 million in residual financial exposure that is not addressed through current regulation. The ability of the State Trust Fund to adequately respond to the remaining exposure is directly related to the number of participants, the value of the operator's individual financial demonstrations, and the amount of money drawn from the State Trust Fund over time.

Staff estimates the State Trust Fund would generate between \$1.8 million and almost \$3.7 million in annual funding, based on participation rates of 50% and 100%, and disposal rates remaining relatively constant. If disposal rates decline or if there are early needs to expend money from the State Trust Fund, it may not increase significantly over time.

## Stakeholder Input

CalRecycle conducted a public workshop on January 28, 2010, to solicit feedback from stakeholders on the implementation and administration of AB 274. Comments received can be classified into three groups: 1) need for additional clarity in the *statutory language*, 2) questions and comments on how CalRecycle would *administer* the law, and 3) *incentives* for participation. In addition, staff pointed out the need to conduct a financial assessment of the State Trust Fund to determine the effect it will have in effectively dealing with financial exposure borne by the state. This analysis is seen as a precursor to the discussion and potential development of any fund participation incentive.

Workshop participants identified a number of implementation areas that would benefit from additional staff analysis to clarify and/or further specify the operation of the State Trust Fund. While some participants suggest regulations, staff believes the requested clarifications to initiate the State Trust Fund can be accomplished by providing templates and other guidance documents. Subsequent regulations can be established, as necessary, after the initial implementation of the State Trust Fund. In addition to the comments regarding clarity in the statutory language, CalRecycle administration of the law, and incentives for participation, stakeholders presented the following points regarding incentives during the workshop:

- Need clarity on what "commitment" means relative to signing up for the State Trust Fund.
- What if a facility is sold after signing up to participate in the State Trust Fund?

- What if a facility goes bankrupt?
- What happens if the only asset an owner/operator has is the landfill? Is CalRecycle going to take over the landfill?
- What kind of oversight will be required on a day-to-day basis?
- Is CalRecycle considering a cap on the State Trust Fund?
- There should be no cap on the State Trust Fund.
- What happens after funds are expended for postclosure maintenance vs. corrective actions?
- Some expressed opinion that the State Trust Fund should not be used for loans.
- What about loans for a temporary default?
- What if there is not enough participation? Will CalRecycle consider additional rulemaking?
- What will terms of participation be?
- Expenditures from the State Trust Fund should not be by the owner/operator who is defaulting; it should be by others like CalRecycle or local government.
- There could be situations where an owner/operator could carry out operations more cost effectively than CalRecycle, but how can this happen without enriching or incentivizing owners/operator to default?

Industry stakeholders indicated that the state benefits from the establishment of the State Trust Fund, because it serves to reduce the state's financial exposure and resulting risk. As such, these stakeholders feel that incentives are needed to induce them to participate in the State Trust Fund. Stakeholders presented the following points regarding incentives during the workshop:

- What incentives will there be for participation in the State Trust Fund?
- Stakeholders believe CalRecycle is asking facilities to put in up to \$75 million, so it should be worthwhile. Why should an owner/operator participate?
- Must have regulations in place that spell out incentives for participation and address some of the administrative issues before facilities have to make commitment to the State Trust Fund.
- Workshop participants suggested the following incentives:
  - Amount of Required Coverage: Consider modifications to the regulations that would substitute the step-down to 15X the annual postclosure cost requirement with a draw-down to 5X the annual postclosure costs.
  - Transfer of ownership: Consider modification to the regulations that require the buyer of a closed landfill to have landfill operational experience to be able to assume reduced financial assurance levels achieved by the seller.
  - Custodial care: Re-examine the concept of "custodial care" that could define how a landfill operator can exit postclosure care, including the requirement to maintain financial assurances.

Upon further review, CalRecycle staff disagrees with the assertion that the benefits of the creation of the identified State Trust Fund should be balanced by further incentives provided to encourage participation by landfill owners in the State Trust Fund. This topic is further explored in the analysis portion.

### **Fundamental Issues**

Staff prepared the following list of fundamental issues that were discussed during the workshop and bear upon the direction CalRecycle pursues to implement AB 274/AB 1004.

### Minimum Participation

AB 274/AB 1004 calls for operators to submit letters of participation by January 1, 2012. Some stakeholders are requesting that they would need to see regulations in place that spell out incentives for participation before they would make a commitment to participate in the State Trust Fund. Other stakeholders are expressing their opposition to any statutory or regulatory changes that could weaken existing or proposed regulatory requirements.

AB 274/AB 1004 provides permissive authority for CalRecycle to adopt regulations. The statute provides sufficient direction for basic implementation of the State Trust Fund without further rulemaking, allowing CalRecycle to implement the statute without making a rulemaking effort. However, CalRecycle may consider establishing standards that provide clarity for the administrative implementation of the State Trust Fund and/or could include participation incentives. In considering whether or not CalRecycle should move forward with regulatory changes, and whether the changes should provide incentives or not, the following dilemma must be considered: operators may not want to commit to the State Trust Fund until they have sufficient incentive to participate and CalRecycle may not want to commit staff resources to a rulemaking not knowing if the resulting regulations will be used. Clearly a process going forward needs to assess stakeholder participation commitment before extensive resources are committed to develop additional regulations.

### Financial Risk Evaluation

If CalRecycle moves forward with consideration of regulatory changes that serve as incentives to participate in the State Trust Fund, it must weigh the potential financial risks [costs] to the state from each of these options. The State Trust Fund balance should be able to cover any additional exposure created by any reduction in financial assurances for those landfill operators participating in the State Trust Fund. Reasonable forecasts of the amount of the fund must take into account factors, such as the fact that participant landfills will close over the life of the State Trust Fund (some after a relatively few years of participation); Waste diversion goals will impact future disposal rates and further reduce the deposits to the State Trust Fund over time; and if the State Trust Fund is drawn upon early in its creation it may not be able to build up substantial cash reserves for out-year needs. Based on disposal data from 2009-2010 and minimum participation in the State Trust Fund, CalRecycle staff estimate annual deposits into the State Trust Fund of approximately \$1.8 million [50% X 30 million tons X \$0.12/ton]. A larger participation rate will augment the amount of the State Trust Fund. A staff analysis and forecast that applies the above concerns along with a range of participation rates and estimates of landfill operator/financial assurance failures that formed the basis of the \$370 million in residual financial exposure is included in this paper to further the understanding of the potential benefits to the state from the implementation of the State Trust Fund.

### Fair Share

Under AB 274/AB 1004 the \$0.12 per ton fee would be paid by operators of active landfills that commit to participate in the payment. CalRecycle, however, may expend money from the State Trust Fund for postclosure maintenance or corrective actions at any active or closed landfill. This raises a potential fairness issue as it relates to the value of a participant's contributions to the State Trust Fund during the active life of the landfill and the benefit of any incentives, if provided, that may reduce the amount of financial assurances the operator must maintain during the postclosure maintenance period. For example, if Landfill A pays in for 2 years, closes, takes advantage of incentives to reduce financial assurances and soon after defaults, that operator would be receiving a disproportionate share of State Trust Fund benefit.

## **Analysis**

### Collection of Fee and Growth of State Trust Fund

The State Trust Fund must take into account factors, such as participant landfills closing over the life of the State Trust Fund (some after a relatively few years of participation); how waste diversion goals will impact future disposal rates and further reduce the deposits to the State Trust Fund over time; and, if the State Trust Fund is drawn upon early in its creation it may not be able to build up substantial cash reserves for out year needs. Based on disposal data from 2009-2010 and assuming minimum participation in the State Trust Fund, CalRecycle staff estimate annual deposits into the State Trust Fund of approximately \$1.8 million [50% X 30 million tons X \$0.12/ton]. A larger participation rate will augment the amount of the State Trust Fund. Almost \$3.7 million in annual deposits could be secured if 100% of operating landfills participate in the State Trust Fund.

By identifying the most likely participants in the State Trust Fund deposit payments without additional incentives (Waste Management and Republic Services); CalRecycle staff can calculate that the represented tonnage is equal to approximately 12.8 million tons, or just over 42% of the 2009-2010 statewide tonnage. [When the complete 2010 disposal year information is available, these calculations will be amended as necessary, but the tonnage is not anticipated to change by a significant amount.] If other larger private operators are added to the calculation, the participation percentage will increase to almost 49%. To move forward with calculations that would ensure that minimum participation levels were met to establish the State Trust Fund, the additional 8% participation was created by adding the Los Angeles County Sanitation Districts to the tonnage represented by Waste Management and Republic Services - bringing the total participation rate to just over 50%. However, it should be noted that the participation of the LA Sanitation Districts has been previously identified as only occurring if the suggested incentive of allowing a reduction from the earned step-down reduction of 15X postclosure maintenance estimates to an annually reduced draw-down all the way to 5X postclosure maintenance estimate. This option is discussed below. Without this incentive, their participation is not certain, as their representatives have previously identified their intent to not participate. As commented, adding the LA Sanitation Districts will bring the total participation level to approximately 50%, allowing the State Trust Fund to be established. However, with just 50% participation, the annual funds raised will only be approximately \$1.8 million. If a couple of counties with a significant amount of disposal, such as Orange County and Riverside County commit to participate, the tonnage committed will represent almost 65% of the 2010 disposal, and the fee will equal approximately \$2.4 million per year. CalRecycle staff caution against the inclusion of any of these public operations, because the representatives from these counties have previously identified that they have no desire to participate in a State Trust Fund, primarily because they believe that their residents will be put in a position to pay for the problems of others throughout the state, and will be unlikely to ever receive benefit from the State Trust Fund without also repayment to the fund.

### Fee Collection Overhead

Staff anticipates no immediate fiscal impact associated with the State Trust Fund. It is important to note, however, that the State Trust Fund would only become operative should the 50% participation threshold be reached and if that were to happen, the revenue of the State Trust Fund would be relied upon to cover any fiscal needs. These fiscal needs will be costs paid to the California Board of Equalization for their direct collection expenses, and CalRecycle staffing expenses spread over the impacted programs of the Legal Office, Financial Assurances Unit, and other administrative impacts.

At the point in time that CalRecycle begins to utilize the State Trust Fund to respond to failures at various landfills throughout the state, additional expenses will arise. The additional staff expenses, paid from the revenues of the State Trust Fund, will include additional Contracting, Accounting, and Legal Office activities to seek out contractors and pay for needed and covered activities. In addition, directly involved

program expenses will be encountered for remediation plan review and implementation, contractor oversight, health and safety activities, monitoring expenses, as well as fund management and disbursements.

The State Trust Fund is anticipated to be a reasonably small fund. If it is reasonably small, the combined overhead and implementation expenses are likely to rise to a significant portion of the annual fees collected. These personnel expenses, in very general terms, are usually estimated at approximately \$100,000 per year per PY, overall. With the State Trust Fund collecting as little as \$1.8 - \$2.4 million annually (based on \$0.12 per ton for approximately 30 million tons disposed and a participation rate of 50% - 65%), the overhead and implementation expenses of the fund are likely to rise to as much as 10-20% of the annual fees collected.

#### Remaining Exposure to State

As identified during the development of the Long-Term Postclosure Maintenance, Corrective Action and Financial Assurances rulemaking - estimates of landfill operator/financial assurance failures (over the next 100 years) are anticipated at \$370 million in residual financial exposure to the state even after the implementation of the rulemaking. Additionally, approximately \$500 million is anticipated for extraordinary corrective action costs that are not financially assured by any operator within the state. Consideration and implementation of any incentive to participate that may further reduce the operator's financial assurances to the state will also further increase the state's financial assurance exposure, because the chances of default of the operator is not impacted by the incentive, but the remaining financial assurance available to the state - when these failures occur - will be diminished. The failures identified in the \$370 million are comprised of a range of temporary defaults by some private operators and some local government operations, as well as permanent defaults of many of the smaller private operations throughout the state. Essentially all of the private owners of only one landfill, where the landfill was the primary business during operation, are anticipated to eventually default and leave the local governments and the state with the final maintenance and care of the facility.

The establishment of the State Trust Fund will maintain the characteristics of a fund attracting the participation of the highest-risk participants (all landfills are covered for corrective action and postclosure maintenance failures) while likely only collecting fees from a few lower-risk participants. With the decline in disposal rates over recent years, and the continued work of CalRecycle to continue the decline in disposal in the future, the nominal fee of \$0.12 per ton, even if collected from 100% of the operating landfills, does not cover the failure exposure anticipated during the extensive modeling of the solid waste system.

#### Operator-Suggested Incentives

1. Amount of Required Coverage: *Consider modifications to the regulations that would substitute the step-down to 15X the annual postclosure cost requirement with a draw-down to 5X the annual postclosure costs.*

Reducing the postclosure maintenance cost estimate multiplier for participants from the lowest "earned" level of 15X to an "automatic" reduction of 5X will increase the exposure to the state. On average, this increase will be as much as three times the current exposure. In dollar value, such a change is anticipated to represent an increase from the current \$370 million exposure to as much as \$1.191 billion.

CalRecycle's decision in adopting the long-term postclosure financial assurance rulemaking requiring closed landfill operators to definitively show that the postclosure plan and maintenance are effective prior to allowing reductions in the postclosure financial assurance demonstration is anticipated to significantly reduce the anticipated financial exposure to the state and the financial burden to a State Trust Fund, should the State Trust Fund be established. The significant reduction in financial demonstrations, simply by opting to participate in the State Trust Fund seems to be greatly overshadowed by the potential

financial risk shifted from the operator to the state. This option shifts a significant exposure to the state, and does not appear to be a viable incentive option.

2. Transfer of ownership: *Consider modification to the regulations that require the buyer of a closed landfill to have landfill operational experience to be able to assume reduced financial assurance levels achieved by the seller.*

Allowance of an operator of a closed landfill to reduce the financial assurance demonstration for postclosure maintenance is based on two basic criteria, depending on the time period that the facility was closed. Operators having exhausted the capacity of the landfill prior to the 2010 effective date of the final rule amendments completed their operations under an expectation and regulations that allow automatic reductions in their financial demonstrations as they progress through postclosure maintenance. CalRecycle limited this reduction to 15X the annual postclosure maintenance estimate to limit the financial exposure burden placed on the state. Operators closing after the effective date of the rule change are required to show that the postclosure maintenance plan is effective, that their maintenance procedures are effective, that the facility is effectively containing the disposed waste, and that they are taking additional steps to ensure that any potential problems are identified early in order to make additional corrections to the maintenance procedures to limit potential problems becoming corrective action issues.

The experience of the operator of the facility, including the experience in maintaining the closed facility, is considered to be critical in the reduction of probabilities for environmental and financial exposures from the facility. CalRecycle specifically recognized that the experience of the operator would impact the exposure of the facility in the adoption of the final rule - requiring additional financial assurances of less experienced operators. To remove this financial requirement from the regulations as an incentive to participate in a State Trust Fund would only increase the potential for the closed facility to be transferred to a less capable operator (i.e., increase the exposure to the state), without having any direct impact on the operators intending to maintain their closed facilities in the best manner possible and protection of the environment foremost in their actions. Identifying such an amendment to the regulations as an “incentive” to participate is not readily quantifiable in this analysis.

3. Custodial care: *Re-examine the concept of “custodial care” that could define how a landfill operator can exit postclosure care, including the requirement to maintain financial assurances.*

CalRecycle staff anticipates continued efforts to increase knowledge of postclosure care and maintenance techniques. Identifying such continued efforts as an “incentive” to participate is not readily quantifiable in this analysis. The ability of the operator to identify reductions in costs associated with postclosure maintenance as the closed facility stabilizes continues to be available to all operators, regardless of participation in the State Trust Fund. Elimination of the financial assurance demonstration requirements is ultimately controlled by the statutory requirement for the demonstration to be maintained until there is no further threat from the waste placed in the facility.

#### Potential Incentive for Consideration

If CalRecycle determines that an incentive is justified to encourage participation in the State Trust Fund, an option to consider is the removal of the requirement to earn the reduction to 15X and allowing all participating landfills owners to annually reduce the financial assurance demonstration for their landfill, on a year-for-year basis, only as long as no corrective action is required at the facility, to a minimum of 15X the annual postclosure maintenance cost estimate. This incentive may provide adequate reduction in anticipated maintenance expenses to balance the projected payments into the fund by the operator to make participation in the State Trust Fund viable for the landfill. The potential cost savings to the operator would be dependent on the site-specific enhanced monitoring program (that would not be required if this incentive were implemented), and their internal savings due to having annual access to postclosure maintenance funds in lieu of applying for access once every five years. The caveat of eliminating any

further multiplier reductions upon a need for corrective action at the closed facility will help maintain a reasonable level of financial assurance for the state.

### **Recommended Plan of Action**

Staff recommends the following course of action to address the implementation of AB 274/AB 1004:

- January/February 2011 – Conclude forecast and financial analysis of the State Trust Fund and of potential fund participation incentives. Advise stakeholders of any viable incentives that CalRecycle may be willing to pursue if fund participation is above 50% (or at a greater percentage if necessary to support them), and staff's analysis indicates that the incentives may result in a positive financial outcome for the state. A positive financial outcome is one in which the state's potential financial exposure is reduced from the level of exposure from the Phase II regulations alone. Conclude discussions and reach an agreement on the State Trust Fund implementation issues identified above.
- March 2011 - Hold a workshop with stakeholders to discuss the results of the staff analysis.
- July 2011 – Receive representations (letters of interest) from industry stakeholders that include their continued interest and commitment in the State Trust Fund.
- September 2011– Upon receipt of letters of intent to participate in the State Trust Fund from at least 50% of the industry, initiate informal rulemaking discussions for any incentives to participate determined in the state's financial interest through the process described above.